No. 13,393

IN THE

United States Court of Appeals

For the Ninth Circuit

FRED G. STEVENOT, Trustee of Coastal Plywood & Timber Company, a Corporation, Debtor,

Appellant,

vs.

J. W. NORBERG, NILS G. MATSON, MERRITT W. TALLMAN, MILO F. BARNHART, ROLAND C. ZIMMERMANN, FLOYD C. JACKSON, GLADYS M. ZIMMERMANN, EDWIN H. JASMANN, FRANK SUTTON, GEORGE F. SCOTT and JOHN E. VICK,

Appellees.

Reply Brief of Appellant

Appeals from the United States District Court,
Northern District of California,
Northern Division

Honorable GEORGE B. HARRIS, Judge Presiding

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INTRODUCTION

This appeal involves two primary issues, viz.:

(1) Did the District Court err in ordering appellant to reinstate appellees as employees of Coastal Plywood & Timber Company (hereinafter called the "Debtor") following their discharge by appellant; and

(2) Did the District Court err in ordering that appellees be reimbursed for wages lost by them during the period of such discharge.

In addition, error is assigned to an order of the District Court directing appellant to file a supersedeas bond and to a further order re-taxing costs.

The primary issues noted above are distinct and separate and should be so regarded in appraising the arguments advanced by appellees to sustain the ruling of the District Court. In this connection, appellees contend that the first of said issues is moot. We shall consider this contention before proceeding to the basic legal questions presented. Before doing so, however, we desire to call to the attention of Your Honors that counsel in his Brief attempts to create the belief that this involves a labor relation contract covered by the California Labor Code or the National Labor Relations Act. Such is not the fact for neither the California Code nor the National Act is involved herein in any respect. This is conclusively shown by the Petition of appellees (Tr. pp. 10-18), filed herein and in which they make no reference to such Code or Act but rely solely and wholly on an alleged contract with Debtor. Appellees are not and never have been under the National Labor Relations Act and the references of counsel thereto as well as the statements of the lower Court that the discharge of appellees was "contrary to sound industrial relations practice" have no bearing whatsoever upon the present issue, based as it is upon a straight breach of contract action. Moreover, the United States Supreme Court has twice held directly that even employees covered by the National Labor Relations Act must keep and live up to their contracts. See—*National Labor*

Relations Board v. Sands, 306 U.S. 332; 59 S.Ct. 508, cited at pages 19 and 21 of our Opening Brief. Also see—*N.L.R.B. v. Fansteel, etc.,* 306 U.S. 240; 59 S.Ct. 409.

ARGUMENT

I.

The Issue as to Reinstatement Is Not Moot

In the Brief of Appellees (p. 3) it is asserted that appellant, in his Statement of Points, takes no exception to that portion of the Interlocutory Order of the District Court requiring appellant to reinstate appellees in the jobs held by them prior to their discharge. Subsequently in the Brief of Appellees (pp. 21-22), it is contended that the issue as to reinstatement is now moot. Apparently, it is the contention of appellees that, because they have been reinstated as employees of the Debtor, as directed by the Order of the District Court, no issue now exists as to whether said Order was proper.

In so contending appellees ignore the first, third, fourth, fifth, sixth and seventh points included in the Statement of Points Upon Which Appellant Intends to Rely on Appeal from said Interlocutory Order (Tr., pp. 29-31). These points assert, in substance, that the District Court erred in (1) denying appellant's motion to dismiss appellees' petition for reinstatement with back pay, (2) granting appellees' petition for specific performance of contracts for personal services, (3) failing to give effect to an amendment to appellees' contracts which sanctioned their dismissal, (4) failing to hold that the discharge of appellees was justified by their prior breach of their contracts with the Debtor, and (5) substituting its judgment for that of the appellant

in the ordinary business operations of the Debtor. These points are obviousy directed at the reinstatement of appellees.

This issue of reinstatement is far from moot. An issue does not become moot while there exists a real controversy involving the rights of the parties. As stated in *Cramer v. Phoenix Mut. Life Ins. Co. of Hartford, Conn.* (C.C.A. 8, 1937) 91 Fed.(2d) 141, at page 144:

> "* * * But if the alleged moot question involves the merits, or the controversy has not ceased to exist, although its status may have been changed by appellee, or where only a part of the controversy has ceased to exist and other questions remain for decision, the appeal will not be dismissed."

See also *Jackson v. Denver Producing & Refining Co.* (C.C.A. 10, 1938) 96 Fed.(2d) 457, 461.

A relatively recent decision of the Court of Appeals for the First Circuit squarely answers and disposes of the contention of appellees. This decision, *Boston & M. R. R. v. Bentubo* (C.C.A. 1, 1947) 160 Fed.(2d) 326, involved the right of a veteran to reemployment. It was held that reemployment pending appeal in order to stop the accumulation of damages does not render the question of right to reinstatement moot.

See also *Walling v. Hemerich & Payne, Inc.* (1944) 323 U.S. 37, 65 S.Ct. 11, 89 L.Ed. 29, holding that the voluntary discontinuance by an employer of "split-day" contracts alleged to violate the Fair Labor Standards Act did not render an action to enjoin use of such contracts moot where "a controversy between the parties over the legality of the split-day plan still remains." (323 U.S. at p. 43.)

Appellant has been compelled to reinstate appellees in the jobs held by them on December 27, 1951, at the Cloverdale plant of the Debtor, or to restore them to substantially equivalent employment at said plant at equivalent rates of pay (Tr., p. 54). The District Court has held that appellees have a contract right to employment, and an inviolable privilege to remain in such employment. Appellant is directed, on the one hand, to conduct and operate the business of the Debtor to the best of his ability (Tr., p. 5); on the other hand, he is compelled to retain certain individuals as employees whatever his business judgment may be as to their ability to perform their jobs. Moreover, he is compelled to retain them in the same or substantially equivalent jobs as those held on December 27, 1951, irrespective of his business judgment that such jobs could better be performed by other employees. In addition, appellant claims that appellees have no such contract as they allege in their petition; that such was abrogated by the amendment of the By-Laws of Debtor upon the 10th of September, 1950. Such claim of appellant is a continuing one and has application to many of his employees not parties to this proceeding, and appellant now seeks the ruling of this Court as to the validity of not only appellees alleged contracts, but to the alleged contracts of such other employees not parties hereto. Therefore, this appeal and the question of its being moot is directly covered by the decisions hereinabove cited, viz: *Cramer v. Phoenix, etc., Boston, etc., v. Bentubo* and *Jackson v. Denver, etc.,* supra. Furthermore, the question of the *damages* allowed appellees by the lower Court is present in all force and depends upon the answers given by this Court to the questions presented herein by appellants. We submit

that the issue of the right of appellees to reinstatement is most real.

II.

The District Court Erred in Ordering Reinstatement of Appellees

Appellees endeavor to justify their reinstatement on two grounds, viz:

(1) The District Court had power to correct improper and unauthorized action of appellant; and

(2) Appellees were entitled to employment under their contracts with the Debtor.

A. APPELLANT'S ACTION WAS WITHIN HIS AUTHORITY AS TRUSTEE FOR THE DEBTOR.

Appellees endeavor to make much weight of their contention that their discharge was not authorized by the Court. *The simple answer to this contention is the fact that appellant was acting within the authority expressly conferred upon him by the District Court of the United States for the Northern District of California, Northern Division.*

Appellant was appointed Trustee of the Debtor by Order of the Honorable Dal M. Lemmon, before whom the proceedings for reorganization of the Debtor pursuant to Chapter X of the Bankruptcy Act are now pending (Tr., pp. 3-8). By said Order, appellant was authorized and directed as follows:

> "It is Further Hereby Ordered that the trustee appointed herein be and he is hereby authorized and directed, pending further order herein, to conduct and operate the business of the debtor and to manage, maintain and keep in proper condition and repair the assets, properties and business of the debtor, wherever

> situated; *to employ and discharge, and to fix, subject to the approval of the court, the rate of compensation of all officers, managers, superintendents, agents and employees;* * * *." (Tr., p. 5) (Emphasis added.)

This Order *expressly* authorized appellant to employ and to *discharge* any officers, managers, superintendents, agents and employees of Debtor. More direct language conferring discretionary authority upon apppellant is difficult to imagine.

The vesting of such authority in appellant was consonant with and pursuant to Chapter X of the Bankruptcy Act. Section 189 of said Chapter X (11 U.S.C.A., Sec. 589) provides, in part, as follows:

> "A trustee of debtor in possession, upon authorization by the judge, shall operate the business and manage the property of the debtor during such period, limited or indefinite, as the judge may from time to time fix * * *."

An important function of a Trustee in reorganization proceedings is thus to operate the business of the Debtor, i.e. to supply the business experience, skills and attention which the court and lawyers necessarily cannot provide. The performance of this function quite naturally must involve a wide discretion, and this is recognized in both Judge Lemmon's Order and the statute quoted above. The operation of a business such as that of the Debtor involves the constant exercise of judgment and discretion. The Trustee having exercised his business judgment in a business matter placed within his province by judicial order pursuant to Chapter X, should the court then substitute its business judgment for that of the Trustee?

B. THE DISTRICT COURT ERRED IN SUBSTITUTING ITS BUSINESS JUDGMENT FOR THAT OF APPELLANT.

The relative positions occupied by the Court and Trustee in bankruptcy proceedings was very ably set forth in *In re Baber* (D.C. Tenn., 1902) 119 Fed. 520, at page 526, as follows:

> "* * * Undoubtedly, by the very terms of the bankruptcy statute, the trustee acts at all times technically under the direction of the court, and no doubt he has on proper occasions and under proper circumstances, the right to apply to the court for its instructions in the premises. Section 47(2). But this does not mean that he can shovel the administration of his trusteeship into the court, unload his responsibility upon the referee, or judge of the court, and evade or shirk his plain duties by asking the advice and directions of the court. Properly he should be a man of affairs, ready to act upon his own responsibility and intelligence, as business men do in their own affairs; * * *"

While the *Baber* decision involved a trustee appointed in ordinary bankruptcy proceedings, the quoted language is even more pertinent in reorganization proceedings, which contemplate continued normal business operation of the Debtor rather than liquidation. *In re Realty Associates Securities Corporation* (D.C. N.Y., 1944) 54 F. Supp. 787, 788.

To the same effect see *2 Remington on Bankruptcy,* Section 1120, page 677, where it is stated:

> "* * * Where a matter rests in the discretion of the trustee, the court, ordinarily, will not instruct him how to exercise his discretion * * *."

See also *In re Moir Hotel Co.* (C.A. 7, 1950) 186 Fed.(2d) 377, 381-2.

Appellees and the District Court have overlooked this fundamental position of a Trustee in reorganization proceedings, as well as the express authority to employ and discharge employees vested in appellant by Judge Lemmon's Order. Their error in this respect is well illustrated by the authorities cited in the Brief of Appellees (pp. 11-14) to sustain their reinstatement. None of these authorities involved an exercise by a trustee of authority clearly within his province. Thus, *In re Howard* (D.C. Cal., 1904) 130 Fed. 1004, *aff'd.* 135 Fed. 721, involved the power of the court to direct a trustee in ordinary bankruptcy to pay a final judgment. Similarly, *Pearson v. Higgins* (C.C.A. 9, 1929) 34 Fed.(2d) 27 concerned the power of the court to determine legal title to, and right to possession of, certain property. In *Imperial Assur. Co. v. Livingston* (C.C.A. 8, 1931) 49 Fed.(2d) 745, the court was concerned solely with the question whether a trustee or receiver in ordinary bankruptcy has an insurable interest in the bankrupt's estate. *Western Pac. R. Corporation v. Baldwin* (C.C.A. 8, 1937) 89 F.(2d) 269 involved an attempt to tie up one of the principal assets of the debtor in a voting trust. And *Freeman Coal Mining Corporation v. Burton* (Ill., 1944) 58 N.E.(2d) 589 concerned action by a trustee which, in effect, constituted a gift of property of the estate.

None of these decisions involved a matter, such as here presented, lying within the business discretion of the trustee, or within the authority expressly conferred upon the trustee. In none of these decisions, nor in any other case, has a court undertaken to *reverse* a business decision made by the trustee. The confusion which would result if every business policy of the Debtor were to be determined in court

is obvious. We respectfully submit that the Court erred in substituting its business judgment for that of appellant as Trustee in the present case.

C. APPELLEES HAVE NO CONTRACTUAL RIGHT TO CONTINUED EMPLOYMENT.

Appellees took the position before the District Court that they have a contract of employment with the Debtor, expressed in its original By-laws, which cannot be amended without their unanimous consent. More specifically, appellees contended, and the District Court held, that the original By-laws of the Debtor conferred upon them a vested right to continued employment which could not constitutionally be impaired by an amendment to such By-laws.

The facts bearing upon this issue were summarized in appellant's Opening Brief at pages 11 to 14, inclusive. Briefly stated, Section 2 of Article V of the original By-laws of the Debtor permitted discharge of a stockholder-employee only by vote of the board of directors, subject to review at a meeting of the stockholders (Tr., p. 197). Article VIII of said original By-laws expressly and specifically provided that said Section 2 could be amended by majority vote of the Class A Stockholders (Tr., p. 200). Said Section 2 was so amended, long before the discharge of appellees, to provide that the general manager of the Debtor "may employ, suspend and *discharge* such agents and employees of the corporation as he may from time to time deem necessary, and prescribe their terms of employment and compensation" (Tr., pp. 47-48).

Appellees thus rely upon a contract of employment which specifically and unequivocally provided that the provisions of such contract relating to discharge could be amended at

any time by majority vote of the Debtor's stockholders. Any rights which they derived from such contract, vested or otherwise, were thus subject to any such amendment. The amendment here at issue was adopted in the prescribed manner, and its language giving the general manager unqualified authority to discharge employees is too clear to be subject to question. How, then, can it be contended that appellees have been deprived of any vested contract rights when their original contract and upon which they charge and rely expressly sanctioned the modification which was adopted? (See *Baldwin v. Miller & Lux* and other authorities reviewed at pages 14 to 20, inclusive, of appellant's Opening Brief.)

Appellees do not and cannot offer a real answer to such situation. An examination of the authorities relied upon by appellees demonstrates the weakness of their position (Appellees' Brief, pp. 16-18). These decisions are clearly not in point here. First, they all involve the *interpretation* of a *general* power of amendment. None of the cases relied upon by appellees involved a *specific* power to amend a *specific* provision, which, as the California Supreme Court held in *Baldwin v. Miller & Lux* (1907) 152 Cal. 454, at page 458, cannot be ignored. See also, *Note,* 8 A.L.R.(2d) 893, 907-909.

Moreover, the first two decisions relied upon by appellees, viz., *Bonnstein v. District Grand Lodge No. 4* (1906) 2 C.A. 624 and *Schack v. Supreme Lodge* (1908) 9 C.A. 584, involved attempts to modify insurance contracts with members of mutual benefit societies under a general power of amendment. The unique considerations present in such a case are readily apparent. *State v. San Francisco Savings & Loan Soc.* (1924) 66 C.A. 53 also presented a situation

readily distinguishable from that now before this Court. The amendment there in question sought to retroactively affect contracts with the depositors of a savings bank, i.e. its *creditors*. As noted in *Wilson v. Cherokee Drift Mining Co.* (1939) 14 Cal.(2d) 56, at page 58, such a case, "dealing with liability to creditors, has no relevancy where, as here, we are concerned with the interrelations of the corporation and its stockholders."

The final decision relied upon by appellees also involved a *general* power of amendment. *Bechtold v. Coleman Realty Co.* (Penn., 1951) 79 A.(2d) 661. Moreover, it is contrary to the settled principles enunciated by the California Supreme Court and the great weight of authority elsewhere. See authorities and discussion at pages 14 to 20 of appellant's Opening Brief. See also *Notes,* 8 A.L.R.(2d) 893, 105 A.L.R. 1452.

The District Court, we respectfully submit, erred in holding that appellees have a vested right to continued employment which may not be constitutionally impaired without their consent; appellees gave such consent when they accepted their stock, with the provision for amendment then in the by-laws. A consent to a change may be given in advance; here there was no revocation of such consent by appellees before or at the time of such amendment.

D. MOREOVER, THE REINSTATEMENT OF APPELLEES CONSTITUTED A DECREE OF SPECIFIC PERFORMANCE OF AN ALLEGED PERSONAL SERVICE CONTRACT.

Appellees apparently do not contend that their alleged contracts are anything more than personal service contracts. As such they fall squarely within the authorities discussed at pages 21 to 24 of appellant's Opening Brief, which

authorities establish that such contracts may not be specifically enforced.

Appellees' attempt to sustain the decision of the District Court by an argument that injunctive relief is a proper remedy for breach of a collective bargaining agreement overlooks two fundamental facts

(1) The authorities supporting such relief do not purport to require the employer to employ *specific* individuals, but merely to abide by *his agreement to bargain collectively;* and

(2) The contracts here presented in no way resemble a collective bargaining agreement.

A "collective bargaining agreement" is "an agreement between an employer and a labor union which regulates the terms and conditions of employment with reference to hours of labor and wages, and deals also with strikes, lockouts, walkouts, arbitrations, shop conditions, safety devices, the enforceability and interpretation of such agreement and of numerous other relations existing between employer and employee." *Railway Mail Ass'n v. Murphy* (1943) 44 N.Y.S. (2d) 601, 605-6. The California Supreme Court used much the same language in describing collective bargaining agreements in *Levy v. Superior Court* (1940) 15 Cal.(2d) 692.

Appellees' alleged contracts contain no resemblance to a collective bargaining agreement. In fact, they lack the primary feature of such an agreement, namely, *collective* bargaining. Moreover, they do not purport to regulate the terms and conditions of employment except to a very limited extent and in a remote sense. Appellees' contention in this respect strains the imagination.

E. APPELLEES COULD NOT BE FORCED TO GIVE UP THEIR SHARES UPON THEIR DISCHARGE.

Appellees express concern that, by reason of their discharge, they could be forced to give up their shares of capital stock of the Debtor. In this connection, the Articles of Incorporation of the Debtor provide that the Debtor shall have the option to purchase shares of any stockholder who ceases to be an employee (Tr., p. 39).

Appellees' concern is without foundation. Appellant has no power to expend the funds of the Debtor to purchase capital stock of the Debtor; appellant's powers relate solely to the conduct of the Debtor's business and the development of a plan of reorganization. All other powers over the Debtor's estate rest with the Court. *Bankruptcy Act,* Sec. 111; 11 U.S.C.A., Sec. 511.

Moreover, appellees have already given options to another to purchase their stock (Tr., pp. 14, 88, 89). And, as shown in appellant's Opening Brief (p. 21), their failure to first offer their shares to the Debtor constituted a breach of their contract which justified their dismissal.

III.

The District Court Erred in Directing Payment of Back Pay to Appellees

With the exception of the issue as to specific performance, all of the foregoing principles are equally applicable to the District Court's award of back pay to appellees. *In fact, the award of back pay can only be predicated upon a decision that appellees have a binding contract entitling them to continued employment.*

Obviously, neither appellant nor the Court has the power to make a gift of the Debtor's property. Only *legal* obli-

gations of the Debtor may be recognized; *moral* obligations have no standing. *Wainscott v. Occidental Building and Loan Assoc.* (1893) 98 Cal. 253, 255; *Soberanes v. Soberanes* (1893) 97 Cal. 140, 146. The Court and the Trustee represent *all* interested parties, not just an isolated group thereof. *In re Otto-Johnson Mercantile Co.* (C.C.A. 10, 1931) 48 F.(2d) 741, 742; *In re Fergus Falls Woolen Mills Co.* (D.C. Minn., 1941) 41 F. Supp. 355.

Accordingly, the District Court had no power to order the back pay award unless such award was in recognition of a *binding obligation* of the Debtor to appellees. It may not be predicated upon a mere reversal by the Court of a decision made by appellant as Trustee. The only obligation asserted by appellees is based upon their contracts embodied in the By-laws of the Debtor and, as we have shown, the discharge of appellees was pursuant to and not in violation of said By-laws.

IV.

The District Court Erred in Ordering Appellant to File a Supersedeas Bond

We agree with appellees that, in view of the stay granted by this Court, this issue is now moot (Appellees' Brief, p. 27). It should be noted, however, that appellees' argument completely overlooks the words "in any case" added to Section 25(b) of the *Bankruptcy Act* (11 U.S.C.A. Sec. 48(b)) subsequent to the decision upon which they rely namely, *Pacific Coast Casualty Co. v. Harvey,* 250 Fed. 952. The rule of that case was based on the fact that the Trustee therein went outside of his district and commenced a plenary action, contrary to the facts herein, and no information as to the

assets of the Debtor company was available to the Court in which such action was pending. Probably one of the reasons for the amendment of Sec. 25-b of the Act by the addition of the words "in any case" was the decision in the *Harvey* case. We submit that Sec. 25-b is clear and plain and means what it states "in any case".

V.

The District Court Erred in Retaxing Costs Against Appellant

As to cost of a transcript of certain remarks of the Court ordered, not by the Court, but by counsel for appellees, for his own convenience, we respectfully submit that the law continues to deny the taxation thereof as costs. *Department of Highways v. McWilliams Dredging Co.* (D.C. La., 1950) 10 F.R.D. 107.

As to the witness fees and mileage, we respectfully refer this Court to the authorities cited at page 29 of appelant's Opening Brief, holding that witness fees and mileage of a party may not be taxed as costs.

CONCLUSION

The decision of the District Court has placed appellant in the impossible position of attempting to comply with two irreconcilable judicial mandates. On the one hand, appellant has been directed by Judge Lemmon to operate the business of the Debtor to the best of his ability. By the decision herein appealed from he is required to maintain appellees in their present or equivalent jobs, though other employees may be better suited therefor. Moreover, the rights declared by said decision to be vested in appellees must also

be considered to be vested in the other stockholder-employees. We respectfully submit that, under the facts and law reviewed herein, this condition must be corrected by a reversal of the decision of the District Court.

Respectfully submitted,

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